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SUPREME COURT, U.S.
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No. 207

In the Supreme Court of the United States

OCTOBER TERM, 1960

JULIETTE G. WEIL, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

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INDEX

	Page
Opinion below	1
Jurisdiction	1
Question presented	1
Statutes and regulations involved	2
Statement	2
Argument	3
Conclusion	6
Appendix	7

CITATIONS

Cases:	
Buckley v. *Commissioner*, 66 F. 2d 394, certiorari denied, 290 U.S. 698	5
Commissioner v. *Owens*, 78 F. 2d 768	5
Ferguson v. *Forstmann*, 25 F. 2d 47	5
General Investors Co. v. *Commissioner*, 348 U.S. 434	3
Hart v. *Commissioner*, 54 F. 2d 848	5
United States v. *Cooke*, 228 F. 2d 667	4, 5
United States v. *De Bonchamps*, 278 F. 2d 127	4, 5, 6
Statutes:	
Internal Revenue Code of 1939:	
Sec. 142 (26 U.S.C. (1952 ed.) 142)	4
Sec. 142(a) (26 U.S.C. (1952 ed.) 142(a))	7
Sec. 161(a) (26 U.S.C. (1952 ed.) 161(a))	3-4, 5, 7
Sec. 161(b) (26 U.S.C. (1952 ed.) 161(b))	8
Sec. 3797(a) (26 U.S.C. (1952 ed.) 3797(a))	4, 8
Internal Revenue Code of 1954:	
Sec. 641 (26 U.S.C. 641)	4, 8
Sec. 7701 (26 U.S.C. 7701)	8
Miscellaneous:	
Treasury Regulations 118, Sec. 39.3797-3	6, 9

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OPINION BELOW

The opinion of the Court of Claims (Pet. 1a–12a) is reported at 180 F. Supp. 407.

JURISDICTION

The judgment of the Court of Claims was entered on January 20, 1960, and a motion for rehearing was denied on April 6, 1960. The petition for a writ of certiorari was filed on July 1, 1960. The jurisdiction of this Court is invoked under 28 U.S.C. 1255.

QUESTION PRESENTED

Whether a life tenant empowered to sell real estate assets is taxable as a fiduciary upon capital gains realized upon such sales.

STATUTES AND REGULATIONS INVOLVED

Sections 142(a)(3), 161(a) and (b), and 3797 (a)(6) of the Internal Revenue Code of 1939, and Section 39.3797-3 of Treasury Regulations 118 are set forth in the Appendix, *infra*, pp. 7-9. Sections 641 and 7701 of the Internal Revenue Code of 1954 are substantially the same as the sections set forth under the 1939 Code.

STATEMENT

The taxpayer was named the life tenant of a residuary estate, with contingent remainders to her children, under the will of her deceased husband. The will provided that she was to "have the right, in her absolute discretion, to sell, mortgage, pledge or dispose of all or any part of said estate, real, personal, or mixed" (Pet. 1a). Any amounts received by her from such sales were to be reinvested, the reinvestments to take the place of the assets of the estate sold by her[1] (Pet. 1a-2a).

During the taxable years 1952-1955, the taxpayer sold various securities held by her under the will as a life tenant, pursuant to the authority granted under the will. Net capital gains were realized on these sales during each of the years involved (Pet. 2a). These capital gains were reported on income tax returns for each of the years involved which were filed in the name of the estate of her deceased husband by the taxpayer. Subsequently,

[1] The will also provided that the taxpayer would have the right to invade the corpus if she found it necessary for her comfortable maintenance and support (Pet. 1a). This right was specifically waived by the taxpayer (Pet. 2a).

the taxpayer filed claims for refunds of these taxes on the ground that she was not taxable either as an individual or as a fiduciary on such capital gains (Pet. 2a–3a).

The Court of Claims, in a unanimous decision, held that the taxpayer was required to pay the taxes in her capacity as a fiduciary, and dismissed her action for a refund (Pet. 7a).

ARGUMENT

The decision below is correct and there is no conflict of decisions or other reason warranting review.

1. There is no controversy in this case about the fact that a capital gain was realized on the sale of the securities (Pet. 3). The only question is whether anyone must pay the tax upon such gain. The taxpayer argues, and we agree, that the contingent remaindermen, unascertained as they were during each of the taxable years, clearly could not be held liable for the tax. Accordingly, if the income is to be taxed, the taxing authorities must look to the life tenant clothed here with the characteristics of a trustee toward the remaindermen. Otherwise, for purposes of the taxing statutes, this income would completely escape taxation, despite the "legislative design to reach all gain constitutionally taxable unless specifically excluded." *General Investors Co.* v. *Commissioner*, 348 U.S. 434, 436.

The court below correctly held that a trust existed within the meaning of Section 161 of the Internal Revenue Code of 1939 (Appendix, *infra*, pp. 7–8). See-

tion 161(a) provides that the taxes imposed on individuals—

> shall apply to the income of estates or of any kind of property held in trust, including—
>
> (1) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and *income accumulated or held for future distribution under the terms of the will* or trust; * * *.
>
> [Emphasis added.]

Moreover, Section 142 requires every fiduciary to make a return, and Section 3797(a)(6) (Appendix, *infra*, p. 8) defines fiduciary as a "guardian, trustee, executor, administrator, receiver, conservator, or any person acting in any fiduciary capacity for any person." Here, the income from these sales was accumulated and held for future distribution under the terms of the will, and petitioner was clearly acting in a fiduciary capacity for the remaindermen.

Petitioner's basic contention, however, is that Section 161 applies to a formal trust and that therefore the income in question is not taxable to anyone because the life tenant in this case is not a formal trustee. Such, indeed, was originally the holding of the Ninth Circuit in *United States* v. *Cooke*, 228 F. 2d 667. But this decision was reconsidered by the Ninth Circuit *en banc* in *United States* v. *De Bonchamps*, 278 F. 2d 127. In *De Bonchamps*, the Ninth Circuit, under a state of facts closely similar to those in the instant case, held that the relationship between the holder of a life interest and the remaindermen possesses the characteristics of a trust within the meaning of Section 641(a) of the 1954 Code (sub-

stantially the same as Section 161(a) of the 1939 Code). Hence, the capital gains received from the sale of the corpus were taxable as trust income to the life tenant as a fiduciary. In reaching its decision, the Ninth Circuit cited with approval the decision below in the instant case, and explicitly rejected its earlier decision in *Cooke*. While no other circuit has ruled on the precise issue presented here and in *de Bonchamps*, many other courts have held that the statute is not limited to the formal trust situation, and have given its terms a generalized construction commensurate with the broad definition of a fiduciary given in the Code. *Hart* v. *Commissioner*, 54 F. 2d 848 (C.A. 1); *Ferguson* v. *Forstmann*, 25 F. 2d 47 (C.A. 3); *Commissioner* v. *Owens*, 78 F. 2d 768 (C.A. 10); *Buckley* v. *Commissioner*, 66 F. 2d 394 (C.A. 2), certiorari denied, 290 U.S. 698. Thus, on the basic issue involved, whether the statute refers only to formal or technical trusts, the courts of appeals are in substantial accord; on the narrower issue presented by this case, whether the life tenant is liable for the tax as a fiduciary, the Ninth Circuit and the Court of Claims alone have decided the question and they are in complete agreement.[2]

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[2] Far from making tax treatment of life tenants depend upon the vagaries of local law, as taxpayer contends (Pet. 5, 8-9), the decisions below and in *De Bonchamps* make clear that, for purposes of federal tax law, a federal concept of what constitutes a trust applies, rather than a local concept. Local law is looked to only to determine the duties and obligations of the life tenant towards the remaindermen. Once so determined, the question becomes whether or not such duties and obligations suffice to make the life tenant a fiduciary under the federal law.

2. The Regulations do not support the taxpayer's position. The Ninth Circuit, in the disavowed *Cooke* case, based its decision in large part upon the manner in which the term "trust" was defined in the Regulations. See Treasury Regulations 118, Section 39.3797–3 (Appendix, *infra*, p. 9). Upon its reconsideration in *De Bonchamps*, however, the court noted that the definition in the Regulations—as its language clearly indicates—was no more than an attempt to distinguish the so-called business trust taxable as an association from the ordinary type of trust. It was not, as the court below agreed (Pet. 6a), directed towards the issue of life tenancies. Thus, contrary to taxpayer's contention (Pet. 7), a regulation of long-standing has not been overruled by the decision below; rather an incorrect interpretation of such a regulation has been rejected. The regulation still stands for the purposes for which it was drafted: to distinguish between business and ordinary trusts.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for a writ of certiorari should be denied.

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AUGUST 1960.

APPENDIX

Internal Revenue Code of 1939:

SEC. 142 [as amended by Sec. 112(b) of the Revenue Act of 1941, c. 412, 55 Stat. 687; Sec. 11(c) of the Individual Income Tax Act of 1944, c. 210, 58 Stat. 231; and Sec. 202(c)(2) of the Revenue Act of 1948, c. 168, 62 Stat. 110]. FIDUCIARY RETURNS.

(a) *Requirement of Return.*—Every fiduciary (except a receiver appointed by authority of law in possession of part only of the property of an individual) shall make under oath a return for any of the following individuals, estates, or trusts for which he acts, stating specifically the items of gross income thereof and the deductions and credits allowed under this chapter and such other information for the purpose of carrying out the provisions of this chapter as the Commissioner with the approval of the Secretary may by regulations prescribe—

* * * * *

(3) Every trust the net income of which for the taxable year is $100 or over, or the gross income of which for the taxable year is $600 or over, regardless of the amount of net income;

* * * * * *

(26 U.S.C. (1952 ed.) 142)

SEC. 461. IMPOSITION OF TAX.

(a) *Application of Tax.*—The taxes imposed by this chapter upon individuals shall apply to the income of estates or of any kind of property held in trust, including—

(1) Income accumulated in trust for the benefit of unborn or unascertained persons or

persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; and

(4) Income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

(b) *Computation and Payment.*—The tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary, except as provided in section 166 (relating to revocable trusts) and section 167 (relating to income for benefit of the grantor).

* * * * * *

(26 U.S.C. (1952 ed.) 161)

Section 641 of the Internal Revenue Code of 1954 (26 U.S.C. 641) is substantially the same.

SEC. 3797. DEFINITIONS.

(a) When used in this title, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof—

* * * * * *

(6) *Fiduciary.*—The term "fiduciary" means a guardian, trustee, executor, administrator, receiver, conservator, or any person acting in any fiduciary capacity for any person.

* * * * * *

(26 U.S.C. (1952 ed.) 3797)

Section 7701 of the Internal Revenue Code of 1954 (26 U.S.C. 7701) is substantially the same.

Treasury Regulations 118, promulgated under the Internal Revenue Code of 1939:

> SEC. 39.3797–3 *Association distinguished from trust.* (a) The term "trust", as used in the Internal Revenue Code, refers to an ordinary trust, namely, one created by will or by declaration of the trustees or the grantor, the trustees of which take title to the property for the purpose of protecting or conserving it as customarily required under the ordinary rules applied in chancery and probate courts. The beneficiaries of such a trust generally do no more than accept the benefits thereof and are not the voluntary planners or creators of the trust arrangement. Even though the beneficiaries do create such a trust, it is ordinarily done to conserve the trust property without undertaking any activity not strictly necessary to the attainment of that object.
>
> (b) As distinguished from the ordinary trust described in the preceding paragraph there is an arrangement whereby the legal title to the property is conveyed to trustees (or a trustee) who, under a declaration or agreement of trust, hold and manage the property with a view to income or profit for the benefit of beneficiaries. Such an arrangement is designed (whether expressly or otherwise) to afford a medium whereby an income or profit-seeking activity may be carried on through a substitute for an organization such as a voluntary association or a joint-stock company or a corporation, thus obtaining the advantages of those forms of organization without their disadvantages. The nature and purpose of a cooperative undertaking will differentiate it from an ordinary trust. The purpose will not be considered narrower than that which is formally set forth in the instrument under which the activities of the trust are conducted.
>
> * * * * *